Board of Housing:

The Montana Housing Act of 1975 created the Montana Board of Housing. The Board is an agency of the State and operates within the Department of Commerce for administrative purposes. Under the Housing Act the Board does not receive appropriations from the State's general fund and is completely self-supporting. Substantially all of the funds for the Board's operations and programs are provided by the private sector through the sale of tax-exempt bonds. The powers of the Board are vested in a seven member Board, appointed by the Governor, subject to the confirmation of the State Senate. The Board provides policy direction to the agency staff, authorizes bond issues, approves development financing and evaluates Board Housing Programs. These programs include the Regular Bond Homeownership Program, Special Set-Aside Homeownership Program, Multifamily Loan Programs, Low Income Housing Tax Credit Program, Housing Revolving Loan Fund and the Reverse Annuity Mortgage (RAM) Program.

The Board of Housing is funded by four enterprise funds with revenues derived from an administrative charge applied to projects and mortgages financed. Under the Montana Housing Act of 1975, the board does not receive any general fund, and is completely self-supporting.

Board of Housing Goals & Objectives:

- Continue automation of functions to improve operations. Continue to look at new ways of operating to improve efficiency and timeliness.
- Manage the assets of the Board in the most effective manner to enhance the ability to provide housing finance for lower income Montanans. Use any program earnings to recycle into new mortgages or call bonds.
- Continuously review programs to determine if they are meeting the needs of the population they are intended to serve. Continue to change program requirements based on current conditions.
- Increase education and outreach to the citizens of Montana and the Board's customers and servicers through public appearances, workshops, print media, and other means as appropriate.
- Provide training to lenders and realtors, as well as work with non-profits to provide rental counseling, homebuyer education, foreclosure prevention and post purchase education.
- Develop and implement creative methods of financing multifamily rental housing.
- Review opportunities for preservation of federally financed housing, and work with HUD on restructuring of multifamily properties when appropriate.
- Find ways aimed at lowering the cost of housing including The Plan Book and The Governor's House Program.
- Develop programs that meet the needs of populations that are not currently being served.
- Promote the use of the funds within the Housing Revolving Loan Account (HRLA).
- Use Internet web page to provide updated information to persons interested in Board activities and programs.

Board of Housing HB 576 Program Description:

The Montana Housing Act of 1975 created the Montana Board of Housing (Board). The Board is an agency of the State and operates within the Department of Commerce for administrative purposes. The powers of the Board are vested in a seven member board, appointed by the Governor, subject to the confirmation of the State Senate. The Board provides policy direction to the agency staff, authorizes bond issues, approves development financing and evaluates Board Housing Programs. These programs include the Homeownership Program, Multifamily Loan Programs, Low Income Housing Tax Credit Program, Housing Revolving Loan Fund and the Reverse Annuity Mortgage (RAM) Program.

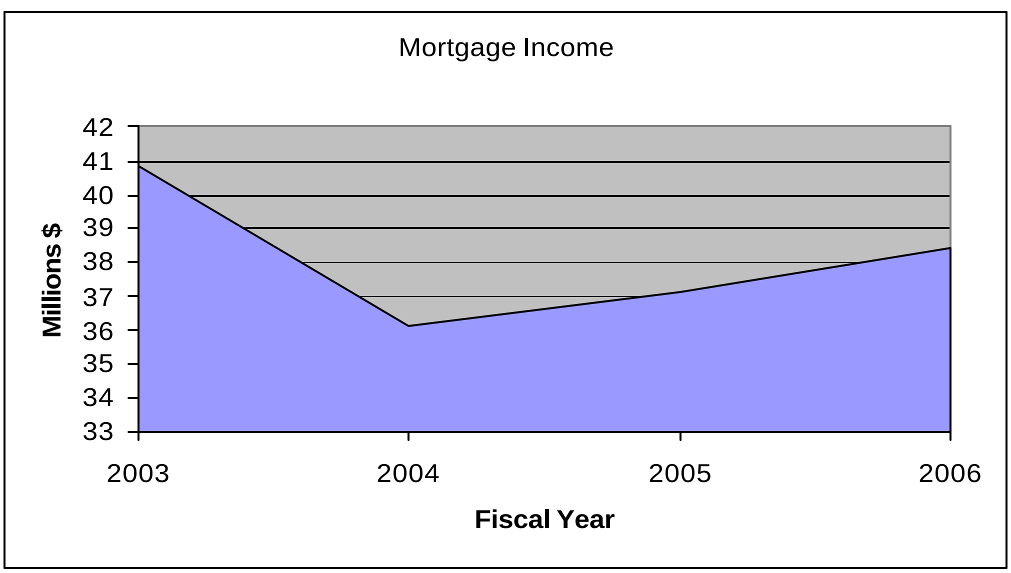
Customers include households that qualify for the Board's programs to either rent or buy their own home. The Board partners with brokers, realtors, banks, real estate lenders, builders, developers, contractors, non-profit housing providers and other governmental entities. Working together with its partners, the Board provides programs that allow a household to rent an apartment or house at an affordable rent. It allows a qualifying household to obtain a lower rate mortgage that will allow them to be able to afford a home that meets their household needs. It also allows qualifying senior households the opportunity to access the equity in their homes to help them afford to stay in their house through a reverse mortgage.

There has not been any significant program, service, or customer base change since the last session. The Board of Housing is primarily mandated in Title 2, Chapter 15; and Title 90, Chapter 1, and Chapter 6, MCA.

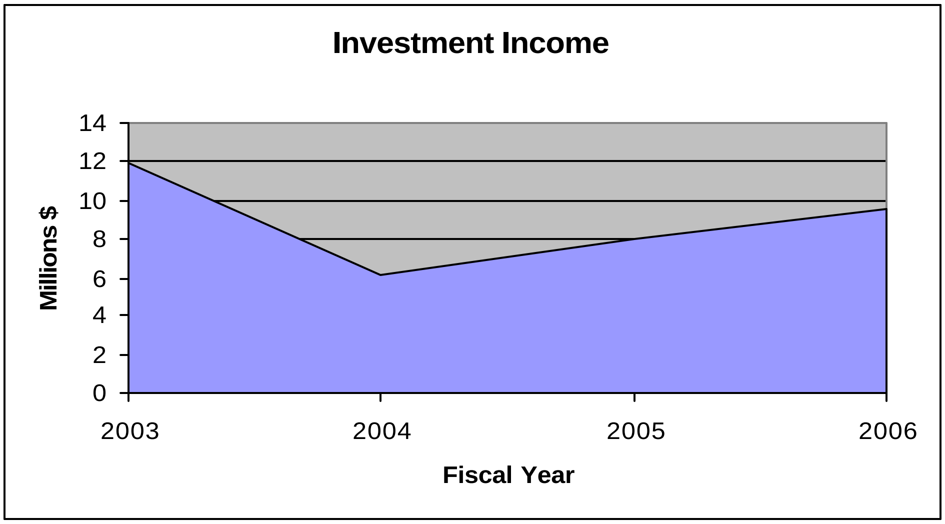
Overview of Board Financial Operations:
Under the Montana Housing Act of 1975, the Board does not receive any general fund money. The Board is completely self-supporting. Substantially all of the funds for the Board's programs and operations are provided by the private sector through the sale of tax-exempt bonds. The Board of Housing is funded by four enterprise funds with revenues derived from an administrative charge applied to projects and mortgages financed.

Revenue Description: Mortgage & Investment Income

About 98% of the Board's income is from Mortgage and Investment income. Mortgage Income is the interest people pay on Board loans used to purchases their homes and is limited by the Internal Revenue Service as a condition of using tax-free bonds as a financing source. Mortgage income is also controlled by the national financial markets which set both mortgage rates and bond financing rates. For example, Board Mortgage income (below) followed financial markets, decreasing until 2004 because national interest rates decreased. In response, people refinanced higher rate Board mortgages with lower rate mortgages and new Board mortgages also had lower rates. This decreased Mortgage Income. Starting in 2005, national interest rates began increasing and Board mortgage income increased.



Investment income comes from interest earned on investing reserves the Board is required to hold and bond and program moneys not yet used to buy mortgages. Investment Income (below) followed the same pattern, decreasing as interest rates decreased, and then increasing as interest rates increased.



Both future Mortgage Income and Investment Income for the Board depend on the interest rate environment which is determined by the national financial markets.

Other Income:
The Board charges the Board of Investments for managing its mortgage loans and for loan cancellations, extensions, or for reviewing certain loan applications.

Board of Housing revenues (accounting entities 06030, 06031, 06078, and 06079) are primarily recorded using the following SABHRS revenue codes:

	FY 2006	%
512033	$ 519.11	0.001%
522017	$ 24.00	0.000%
525130	$ 31,780.00	0.069%
526062	$ 283,794.80	0.617%
530014*	$ (2,958,274.74)	-6.433%
530025	$ 34,960.27	0.076%
530223	$ (10,299.21)	-0.022%
531626	$ (607.04)	-0.001%
531644	$ 609.58	0.001%
538002	$ (40,000.28)	-0.087%
538025	$ 5,557.70	0.012%
538040	$ (3,144.10)	-0.007%
538041	$ 38,556,850.58	83.845%
538042	$ 9,583,642.56	20.841%
538046	$ 4,840.94	0.011%
554040	$ 65,000.00	0.141%

584001	$ 6,475.00	0.014%
584010	$ 975.00	0.002%
593410	$ 186,332.38	0.405%
599001	$ 236,603.80	0.515%
Totals:	$ 45,985,640.35	100.000%

* Investment Income includes Government Accounting Standards Board (GASB) market value adjustment. GASB 31 requires that long-term investments be valued at market and any changes since the previous year be added or subtracted from Investment Income. Since no actual gain or loss occurs, this adjustment artificially affects the Investment Income amount presented. For example, during 1998, the first year that GASB 31 was implemented, the Board recorded an unrealized gain of approximately $2.8 million. In FY2006 the amount was unrealized loss of $2.9 million. In any one year the difference depends on the market. If investments are sold on the valuation date we would have a realized gain or loss, however the Board holds long-term investments until maturity. At maturity, the investment pays off and there is no market gain or loss.

Rate Explanation:

Income Detail by Program:

The Board recovers its costs from charging application and compliance fees for the Low Income Tax Credit Program and from charging a spread on our loan programs. The Board draws funds for its budget from the amounts available within the Indentures. The amount of the approved budget, less any cash on hand, is withdrawn from the Indenture and is allocated among the various Indentures. Any income the Board earns is used to fund special programs that meet the needs of Montana families that are not being met by our regular programs. These funds are pledged to the bondholders.

Homeownership Charges:

According to state statute and, in some cases, the Internal Revenue Code, the Board is allowed to earn the amounts that are presented on the "Report on Internal Service and Enterprise Funds". The Board earns the bulk of its income from the spread between the interest yield on the Single Family Mortgage loans and the yield on the bonds. The Board is allowed to earn 1 1/2% on Pre 1980 Single Family Programs and 1 1/8% on the Post 1980 Single Family Programs.

Financial institutions used to originate Single Family loans for the Board may charge two points, which they keep or originate loans with no points, at a slightly higher rate and have the loans purchased at 102%. Approximately 1% of the loans have 2 points charged. According to tax law, origination points must be included in the amount that the Board can earn. Operating expenses and servicing fees must be paid from the 1 1/8% that the Board is allowed to earn. Servicing fees are .375% of the mortgage principal balance. The Board does not always receive the full 1 1/8% or 1 1/2% spread. The spreads for the last several bond issues were as follows:

* 1996A - 1.125%
* 1997A1 - 1.39063%
* 1997A2 - 1.08842%
* 1998A - 1.10078%
* 1998B - 1.04678%
* 1999A - 1.11985%
* 2000A - 1.10302%
* 2000B - 1.11709%
* 2001A - 1.11898%
* 2002A - 1.12251%

* 2002B - 1.09666%
* 2003A1 - 1.21126%
* 2003A2 - .07883%
* 2003B1 - 1.45392%
* 2003B2 - .51062%
* 2003C - .83833%
* 2004A - .82319%
* 2004B - .49576%
* 2004C - 1.01778%
* 2005A - .89501%
* 2005RA - 1.0336%
* 2005B - .81353%
* 2006A - .8008%

Operating expenses and servicer fees further reduce the amount of these earnings. The 1 1/8% or 1 1/2% that the Board can earn is based on certain assumptions at the time the bond issue is structured. One of the assumptions is that the loans will prepay at 100% of the historical FHA prepayment rate. If the loans actually prepay faster, the Board will not earn the initial spread that was calculated. The Board only earns this spread if the loans are held for the amount of time that is originally estimated. If the loans prepay early, the money is invested and then is used to redeem bonds. When the mortgages pay off, the Board has lost the ability to earn the spread between the mortgage yield and bond yield. Historically, prepayments on the majority of the loans have been over 100%, and we expect this trend to continue.

The Board also charges a cancellation fee of 1/2 of 1% of the loan amount reserved. Approximately 5% of loans reserved are canceled. This amount is included in the spread that the Board can earn. These fees are capitalized and are amortized as income over the life of the loans, as required by generally accepted accounting principles. Extension fees and late fees are also, occasionally, charged. The majority of these fees are capitalized and amortized over the life of the loans. The extension fees are 1/4 of 1% of the loan amount and the late fees are 1/2 of 1% of the loan amount. The amortization of these fees results in an average of approximately $250,000 of income per year. These fees are deposited with the trustees and are used to originate new mortgages.

Multifamily Charges:
Multifamily Programs can earn 1 1/2% spread between the mortgage yield and the bond yield. On the last several issues, the Board did not receive the full 1 1/2% spread. The spreads for the last three bond issues are as follows:

* 1996A - .826%
* 1998A - .28156572%
* 1999A - 1.013963%

(Servicing fees and operating expenses further reduce the amount of this spread.)

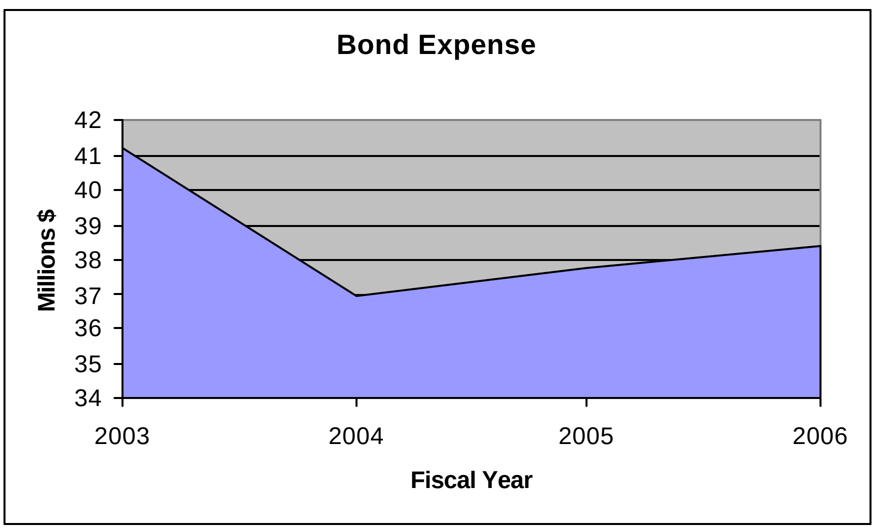
Low Income Housing Tax Credit Charges:
The Board receives approximately $2.1 million dollars of tax credit allocation, annually. The Board charges 4 1/2% of the amount of tax credit reserved. In the next biennium, reservation fee income is estimated to be approximately $94,500 per year. The Board is also required to monitor the projects that receive tax credits to determine if the projects are in compliance with tax credit regulations. The Board charges $25 per unit for compliance fees. The Board has approximately 4,500 units. Approximately $112,500, annually, will be received during the biennium. Tax credit fees are charged to cover the operating expenses of the program.

Housing Revolving Loan Account Charges:
The 1999 Legislature established this fund to provide loans to projects providing affordable housing in Montana. Although the fund was established in 1999 it was not funded. The 2001 legislature added funding through a transfer of Section 8 reserve funds and an allocation of Temporary Assistance to Needy Families (TANF). The TANF funding is currently used to finance down payment and closing cost loans for homebuyers. The other funding is available for other types of housing loans that will typically need that last small piece of financing to make them feasible. The interest that will be charged on HRLA loan will range from 2% - 6%.

Reverse Annuity Mortgage Loans (RAM) Charges:
Under the RAM program, elderly homeowners can receive monthly payments, for 10 years, to assist them with their living expenses. The loans accrue interest at 5%. The principal and interest is not due until the borrower dies or sells their home. It is difficult to determine how much of the interest and principal will actually be received on these loans or when it will be received. These loans are not guaranteed or insured.

Expenses Description: Bond Debt, Loan Servicing and Operations

The Board issues (sells) bonds each year to purchase new mortgages. Once the bonds are sold, the Board must repay the bondholders by making interest and principal payments. The Board is required to use Mortgage and Investment Income to pay bondholders, buy mortgages or pay operating costs. Bond Debt payments are the Board's greatest expense, 88 % of total expenses. Bond Interest rates vary (below) and respond to the interest rate environment set by the national financial markets. As with the previous section, Board rates move with the market. When market rates increase, expenses for bond debt also increase.



The remaining 12 % of expenses are for Loan Servicing and Operations. As shown in the following table, greater than half of Servicing and Operations expenses pay for professional services to banks, mortgage companies and other professionals for issuing bonds, selling mortgages, collecting the monthly mortgage payments, legal services and paying bondholders. The remaining expenses pay for the Board's staff* and staff operations including purchasing and recording mortgage loans, recording repayments and prepayments, investing funds, issuing and redeeming bonds, operating all loan programs and bookkeeping for over 11,000 mortgages, 300 investment accounts, and 31 bond series.

	FY 2006	%
FTE	20.50	
Personal Services	$ 978,777.38	2.226%
Operating Expenses	$ 4,155,333.81	9.452%
Grants	$ 247,404.54	0.563%
Debt Service	$ 38,582,778.33	87.759%
Total:	$ 43,964,294.06	100.000%

*The Board currently operates with a staff of 20.50 people in 20.50 Full Time Equivalent (FTE) positions. Fiscal Year (FY) 2006 Servicing and Operations expenses are for SABHRS Funds 06030, 06031, 06078, and 06079.

Working Capital Discussion:

Collection Of Mortgage Payments & Purchase Of Loans:
Each month the Board receives funds from the financial institutions that service the Board's Single Family and Multifamily loans. The funds include the amount of principal, interest, less servicing fees (.375%, .125% and .10% of the principal balance) that are due on the Board's loans. The Board's trustees collect the money. Twice monthly, the Board purchases loans from new bond proceeds, prepayments or other revenues.

The Board receives tax credit reservations fees when the tax credits are approved. These fees are deposited with the state treasurer and are used to cover expenses of the program. Reservations fees on the Single Family and Multifamily Programs are deposited with the trustees when the approved loans are reserved. They are deposited in the program acquisition account and are used to originate new mortgages.

Payment of Bond Debt:
Principal and interest, on the Multifamily and Single Family Bond issues, is due on each February 1, June 1, August 1, and December 1. Scheduled Debt payments for 2007 are $50,624,869; 2008 are $52,049,419; and 2009 are $52,819,204.

Investments:
The deposit of the initial bond proceeds, used for purchasing loans, is normally invested in a fixed-rate guaranteed investment contract. All debt service reserve funds and mortgage reserve funds that must be held as security for the bondholders are invested in long-term securities, repurchase agreements or guaranteed investment contracts. Under the Multifamily Program, the funds are invested to the next debt service date or to a loan purchase date.

Other Mortgage Purchases:
The Board purchases Reverse Annuity Mortgages (RAM). The RAM loans are not repaid until the borrower dies or sells their home. These amounts are assets of the Board and the interest is accrued monthly, but we may not receive the principal and interest repayments for many years.

The Board also purchases out of the Housing Revolving Loan Program. These loans can be due on sale or amortizing. These amounts are assets of the Board and the interest is accrued monthly.

Fund Equity and Reserved Fund Balance:

Net Assets/Restricted Net Assets:
As stated in the Board's financial statements, Note 1, Fund Accounting: Net Assets – Restricted for Bondholders represent bond program funds that are required to be used for program purposes as prescribed by individual bond indentures. The following are restrictions on the Restricted Net Assets: Special trust funds and accounts within the indenture are pledged as collateral for the bonds under the individual program indentures; Reserve requirements on cash and investments; Mortgage loans receivable are also pledged as security for holders of the bonds; Certain indentures require asset-liability coverage ratios be met as well as cash flow certificates be furnished for any significant change anticipated in the financial structure of an indenture.

The Trust Indentures entered into by the Board requires all mortgages, and all moneys and investments within the indentures are legally restricted to uses provided for in the indentures and fund balance associated with the indentures is legally required to be reserved for those uses.

In addition to the legal requirements mentioned above, the Board commits funds to various projects and programs throughout the year. The Board has set aside over $200 million of first mortgage funds for special programs. In FY 2006, the Board originated approximately $ 28.5 million of loans under this program to households with an average income of $ 28,200, which is below 60% of the median income of the state. As of the end of FY 2006, the Board had $21,329,479 in outstanding Recycled Mortgage Program commitments.

The Board's budgeted monies (those projected to be needed for the fiscal year's operations) are drawn down from the indentures during the fiscal year. These funds are legally pledged to the trust indentures from which they were drawn and any associated fund balance is reserved for the program from which the budgeted funds were withdrawn.

Management Objectives Regarding Fund Balance:
The major component of the Board's Fund Balance (Retained Earnings) is its single-family program. The Board has been recycling repayments and prepayments of mortgages for several years. The Board has committed these funds to special programs, at rates that are in many cases below the average coupon on the bonds. The average income on the special programs is less than $27,000, whereas the average income on the Board's regular bond programs is about $38,000. The Board intends to continue these special programs as they serve Montana citizens the Board would not otherwise be able to serve.

Net income over and above bond debt service, operating costs, and servicing fees, is used to write down the rates on special programs or to fund programs such as the RAM Program for elderly. These programs cannot be funded from direct bond proceeds, as there is no repayment guarantee. In the Multifamily area, the Board intends to continue to leverage its multifamily funds into new multifamily loans through the revolving pool so that loans can be completed in a timely and efficient manner.

The Board is reviewed at the time of each bond issue by two rating agencies: Standard & Poor's, and Moody's Investor Services. In order to meet the cash flow tests, the Board must have sufficient assets, earnings, and liquidity, to meet all bond interest and principal expenses, as well as pay operating expenses. The Board just received an Aa1 from Moody's and an AA+ from Standard & Poor's on its largest indenture. The Board's rating reflects the rates the Board gets on its bonds, which is reflected in the mortgage rates passed on to first time home buyers in Montana.

Rate Explanation:

The Board recovers its costs from charging application and compliance fees for the Low Income Tax Credit Program and from charging a spread on our loan programs.   The Board draws funds for its budget from the amounts available within the Indentures. The amount of the approved budget, less any cash on hand, is withdrawn from the Indenture and is allocated among the various Indentures. Any income the Board earns is used to fund special programs that meet the needs of Montana families that are not being met by our regular programs. These funds are pledged to the bondholders.